Review of the UK Securitisation Regulation: A call for evidence

Insight Investment response

September 2021

BNY MELLON | INVESTMENT MANAGEMENT

Insight Investment manages c.£741.9bn of assets[1] for institutional clients such as pension schemes and insurance companies. Our client base is predominantly defined benefit UK pension schemes and we specialise in providing asset and liability management solutions for these clients, including many of the largest pension schemes in the UK. This involves Insight Investment investing, as investment manager for and on behalf of the various funds / investment vehicles it manages and / or clients it advises ("**Insight**") in securitisation positions across the full range of asset classes, across multiple jurisdictions and in both the public and private markets.

We welcome the consultation by HMT on this important topic and are happy to support HMT in this process. Please find below our responses to the consultation questions.

OVERALL EFFECTS OF THE SECURITISATION REGULATION

1. What are your considerations for investing in an STS versus non-STS securitisation?

Insight Investment, as investment manager for and on behalf of the various funds / investment vehicles it manages and / or clients it advises ("**Insight**"), is not materially affected by whether a securitisation is classified as an STS or non-STS securitisation position. This is primarily because the funds / investment vehicles, and the majority of clients on whose behalf Insight Investment invests, do not obtain the preferential regulatory capital treatment that investing in an STS-compliant securitisation would otherwise afford.

That said, notwithstanding Insight doesn't obtain preferential regulatory capital treatment under the Capital Requirements Regulation, prior to investing Insight Investment does consider the following STS versus non-STS factors (amongst others):

- Insight Investment is required to undertake additional verification requirements under the UK Securitisation Regulation ("**Sec Reg**") when investing in an STS securitisation, so this resulted in an administrative burden;
- the effect, if any, on selling a non-STS securitisation in the secondary market (i.e.: any scenarios in which liquidity could be reduced, or pricing affected, for a non-STS securitisation position compared to had that position been an STS securitisation); and
- whilst the credit analysis for an STS and non-STS securitisation position are generally the same, Insight does gain additional comfort from the legal perspective with respect to transaction structuring, legal documentation, validly, enforcement and legal opinion coverage.

2. What impact, if any, has the Sec Reg had on your investment decisions for investing in a securitisation position, and why?

We've considered this question in some detail, and we generally don't feel that the implementation of the Sec Reg has affected our investment decisions for UK and / or EU issuer or originated deals. However, due to jurisdictional ambiguity, it has often adversely affected our ability to invest in some third country transactions (which we discuss in more detail below).

In general terms, as a leading global asset manager, Insight Investment had always undertaken detailed credit analysis prior to the Sec Reg for each securitisation position it purchased. We also ensured that each transaction had detailed reporting and ongoing transparency requirements. So, in one sense (and we suspect some other asset managers would feel the same) the Sec Reg hasn't enhanced or improved the credit analysis and / or the due care taken prior to purchasing a securitisation position.

In some cases, it has restricted our ability to invest in scenarios where we don't believe it was the intention of the regulators for the Sec Reg to have that effect. For example, the definition of securitisation is very broad and different law firms may have different views on what constitutes a securitisation (for example, in the NPL or trade receivables space). The ambiguity around the jurisdictional scope of the Sec Reg (notably Article 5(e)) has also had an adverse impact.

[1] As at 30 June 2021. Assets under management (AUM) are represented by the value of cash securities and other economic exposure managed for clients. Figures shown in GBP. Reflects the AUM of Insight, the corporate brand for certain companies operated by Insight Investment Management Limited (IIML). Insight includes, among others, Insight Investment Management (Global) Limited (IIMG), Insight Investment International Limited (IIIL), Insight Investment Management (Europe) Limited (IIMEL) and Insight North America LLC (INA), each of which provides asset management services.

3. What changes to the Sec Reg would encourage you to invest more in securitisations of SME exposures?

As the majority of our funds / clients have some nexus to the EU, Insight Investment has to ensure compliance with the EU Sec Reg. However, as a UK investment manager, due to the definition of 'institutional investor' in the UK Sec Reg, Insight Investment also has to comply with the UK Sec Reg. Currently, as the EU Sec Reg and UK Sec Reg are substantially the same, and as a result of the helpful equivalence provisions and differing requirements for third-countries, this has broadly speaking not prevented us from purchasing any securitisation positions. However, should the EU Sec Reg and UK Sec Reg materially diverge, and the transactions are unable to comply with the both regulatory regimes, this will create issues in the market for both SMEs and investors, resulting in reduced access to funding for SME exposures.

MARKET FUNCTIONING

4. How, in your view, has the introduction of the Sec Reg affected the UK's securitisation market since it took effect on 1 January 2019?

Generally speaking, we feel it has increased administrative and operational burdens on originators, sponsors and institutional investors. Legal costs have also increased considerably. As noted above, Insight Investment has always undertaken detailed due diligence, credit analysis and mandated reporting and transparency obligations from applicable third parties, so the due diligence and transparency requirements under the Sec Reg haven't affected how we invest to any real extent, aside from the increased administrative and legal costs involved. It has also restricted / reduced the number of deals we have been able to invest in due to ambiguity in its geographical scope.

5. In your views, has any ambiguity around the geographical scope of the Sec Reg's requirements impeded securitisation transactions? If so, what clarifications could be helpful?

The ambiguity around the geographical scope of the Sec Reg's requirements is one of the biggest issues we have to contend with and has adversely affected our ability to invest in third country transactions. This is especially the case with respect to private bi-lateral and club transactions.

Prior to the implementation of the Sec Reg there was frustration in the market that the US and EU / UK risk retention regimes didn't align, this has now been compounded with the implementation of the EU / UK Sec Regs and the differing and more onerous reporting requirements.

We feel market participants are broadly fine with agreeing to comply with the UK risk retention regime. However, the issues mainly revolve around the Article 7 requirements, especially if that jurisdiction or asset class already has its own governing body or a market agreed form / scope of report, as the case may be (for example, the US CRE CLO market has its own comprehensive form of investor report). Third country issuers / originators are not willing, or are unable, to provide two or more forms of investor reports to comply with the terms of the UK Sec Reg (and EU Sec Reg). We feel this clarification would be most helpful.

6. How do you think the UK securitisation market has performed in comparison to other jurisdictions, both a. Since the GFC, and b. In response to Covid-19?

We feel that as a result of HMT's timely intervention and the various measures it introduced to assist companies during Covid-19, the UK securitisation market has performed well.

7. If you have not originated, issued or invested in an STS compliant securitisation yet, what were the main reasons?

Not applicable. Insight Investment has invested in STS compliant securitisations.

8. If you have previously chosen not to designate a securitisation as STS even where the transaction was likely to qualify as STS, what were your reasons?

Not applicable**.**

9. What are currently, in your view, the main impediments to the growth of the UK's STS market?

No comment.

CONTRIBUTION TO THE REAL ECONOMY

10. How do you think securitisation could better support the financing of the real economy, in particular SMEs? What specific measures would support this?

One of the ways in which securitisations could better support the financing of the economy, especially SMEs, is if transaction costs associated with implementing a securitisation could be reduced. SMEs often find the costs involved prohibitive, especially the structuring, arrangement and legal costs involved, along with the appointment of third parties. Unlike the loan market, which has form documentation suggested by the Loan Markets Association and which are broadly utilised by market participants, there is no form securitisation documentation. On the one hand, if not properly implemented this could cause a raft of additional issues and we don't underestimate the difficulty involved in getting market participants to agree to use more standardised transaction documents (which could be amended for each transaction), but on the other hand it would be ultimately helpful if the industry had some standardised transaction documents that it had the option of using.

INTERCONNECTEDNESS AND FINANCIAL STABILITY

11. How, in your view, has the introduction of the Sec Reg affected the interconnectedness of financial institutions in the UK?

We don't feel the introduction of the Sec Reg has particularly changed the interconnectedness of financial institutions in the UK.

12. How could the Sec Reg do more to address the risks that securitisation activity in the UK poses to financial stability?

We don't feel there is anything substantive that can be additionally undertaken.

OTHER FACTORS

13. To what extent have different Covid-19 measures affected the performance of the UK securitisation market?

We feel HMT reacted quickly to Covid-19, and along with the Covid-19 measures it implemented, assisted greatly with on-going performance of the UK securitisation market.

14. How, in your view, has EU Exit impacted the UK securitisation market

We don't feel the EU Exit has currently impacted the UK securitisation market. As noted above, this is primarily because both regimes substantially run in parallel. Issues will arise, however, when either market diverges from the other regime.

RISK RETENTION

15. Does the risk retention framework effectively balance prudence and market functioning? If not, how could it be improved?

Answer requested by HMT to be given by manufacturers and not investors. No comment.

16. Which modalities do you use and what motivates this? How many securitisations (volume & value) have you used each modality for?

Answer requested by HMT to be given by manufacturers and not investors. No comment.

17. Do you consider the risk retention modality when making investment decisions?

Yes, the risk retention modality is considered and noted. Depending on the asset class, type of investment, in some circumstances pricing / advance rates may be affected if Insight Investment was not satisfied with the modality being provided. However, as a general point, risk retention is not something Insight Investment comes across an issue with.

18. What is the impact of the risk retention rules on securitisations of NPLs?

No comment.

19. In light of the PRA's ongoing consultation on the securitisation of NPLs, would the effectiveness of NPL securitisation be enhanced if the servicer was allowed to fulfil the risk retention requirement?

No comment.

DISCLOSURE REQUIREMENTS FOR PRIVATE SECURITISATIONS

20. What are your considerations in deciding whether to issue a private or public securitisation?

Answer requested by HMT to be given by manufacturers and not investors. No comment.

21. What are your considerations in deciding where to list your securitisation, both in the UK and in other jurisdictions?

Answer requested by HMT to be given by manufacturers and not investors. No comment.

22. How do the costs and benefits of listing securitisations vary by jurisdiction?

Answer requested by HMT to be given by manufacturers and not investors. No comment.

23. Do you consider the disclosure requirements (both the content and format) for private securitisations to be sufficiently useful? If not, how could they be improved? Please answer with reference to:

a. Bilateral securitisations;

b. Intragroup securitisation transactions; and/or

c. Any other private securitisation transactions.

Our responses for each of the above are generally the same, in that the Article 7 disclosure requirements are often onerous for private transactions and dissuades originators and issuers. From our experience, the originators / issuers are unable to provide all the necessary data fields and the form of templates required places a disproportionate administrative and operation burden on private securitisation. It also significantly increases legal costs. Often our investment team requires separate / additional reporting in order for them to undertake their credit analysis and review of the transactions on an ongoing basis, so in some instances the provision of the reporting, as set out in the templates, is provided (to the extent possible) in order to satisfy a 'tick box' approach, as opposed to it being used by investment teams for their analysis (as separate reports are used for this).

24. Do you find the usefulness and quality of the information you receive on a securitisation to be materially different when available through an SR, to when it is not made available through an SR?

No, we have not found this to be an issue. For private securitisations we actually find it preferable to receive information directly from the issuer / originator / sponsor (as applicable) and to be able to communicate directly with the applicable third parties (ie: request additional information not on the templates, query information and to maintain a dialogue with applicable parties). The use of an SR would fetter this important communication channel, especially with respect to bi-lateral private transactions (where there is no arranger / sponsor acting as a go-between), SME deals and new issuers.

25. Does the fact that a securitisation is not reported through an SR impact your ability or willingness to assess credit risk and/or invest in a securitisation?

No, please note our answer for question 24. For private securitisations it is preferable to receive information directly from the issuer / originator / servicer.

26. Do you consider there would be any benefit to extending disclosure requirements for public securitisations to private securitisations, specifically: a. The requirement to make information available through SRs; and/or b. The requirement to fill in the templates on inside information or significant event information, as contained in Annex 14 and Annex 15 of the onshored Technical Standards?

No, for the reasons set out in our answers to questions 24 and 25 above.

STS EQUIVALENCE REGIME

27. To what extent has your firm benefitted from the temporary recognition of EU STS by the UK?

Insight Investment has greatly benefitted from the recognition of the EU STS by the UK. Notwithstanding, as set out in our answer to Question 1, that Insight Investment does not materially benefit from an STS designated securitisation position, due to Insight Investment, as a UK investment manager, having to comply with the UK Sec Reg, it would have been difficult to invest in transactions had this recognition not being provided for.

28. To what extent has a lack of recognition of UK STS by the EU impacted your firm?

It hasn't currently directly affected Insight Investment, but could affect liquidity and pricing in the secondary market should we wish to sell any affected securitisation position.

29. Do you have views on the merits, as well as any drawbacks, of HMT introducing an STS equivalence regime?

We think it would be hugely beneficial if the HMT introduced an STS equivalence regime. This would allow us to continue investing in STS transactions.

30. Are there any mechanisms other than an STS equivalence regime which, in your view, would give effect to the policy objectives in paragraph 5.7?

No comment.

31. Do you have comments on the considerations relevant to making equivalence assessments under a new STS equivalence regime, as outlined in paragraphs 5.16 to 5.22?

No comment.

32. Do you consider an adaptation period accompanying any potential withdrawal of equivalence would be useful in the operation of a new equivalence regime for STS securitisation?

Yes, we feel it would be useful and necessary for the market to function. However, our strong preference would be for the equivalence regime to continue in some form as withdrawal of equivalence would affect our ability to invest.

33. If so, would it be desirable to introduce standardised adaptation periods for STS, or are there other factors which should be considered?

As noted above, our strong preference is for the STS equivalence regime to be extended.

34. Do you have any other views related to STS equivalence which you think should be considered?

We think it would be disadvantageous if the regimes diverged and strict compliance was required. This would affect liquidity, increase costs, and create a barrier with respect to securitisations we could invest in.

ENVIRONMENTAL DISCLOSURE REQUIREMENTS

35. In respect of current disclosure on residential mortgages and auto loans and leases: a. Is the environmental performance data on a securitisation's underlying exposures which you currently receive sufficiently useful? b. What other information would you find useful, if any?

Environmental, social and governance disclosures across all asset classes and types of transactions are of huge importance to Insight Investment. Environmental disclosures are however, best served outside the Sec Reg and should be encompassed within their own regulatory regime, along with social and governance disclosures (ie: under the remit of the UK's climate-related reporting rules adopting the Task Force on Climate-Related Financial Disclosures (TCFD) standards).

We feel that securitisation and non-securitisations should not be distinguished when it comes to provision of ESG information. Not only on the basis of the importance of investors receiving disclosure on underlying assets for financial transactions, but it will likely cause market issues if there are two regimes running in parallel (ie: ESG disclosures required under the UK's adoption of the TCFD rules and then additional / separate disclosure under the Sec Reg).

Another issue with requiring separate Sec Reg disclosure, is that the required disclosure needs to be requested from parties at the underlying asset level and not at the SSPE level (which is reliant on information it receives at the asset level). Also, in a securitisation there can be a time lag as to origination of the underlying exposure and when that asset is securitised. The SSPE is reliant on information it receives from the underlying originator / servicer and is therefore affected by its own ability to report on an underlying asset.

For legacy securitisation transactions where this data is not available, there is no corporate entity as issuer for investors to engage with to request the data. Therefore, legacy securitisation transactions should be considered to be out of scope for ESG rules.

36. In respect of underlying exposures other than residential mortgages and auto loans and leases: a. Are there other types of underlying exposures for which you would find it useful to have information on their environmental impact? If yes, which ones? b. What information would you find useful?

Please see answer to question 35 above.

37. Generally: a. How attractive, relative to other investable ESG securities, are securitisations that disclose environmental performance information?

Please see answer to question 35 above.

38. What additional readily available information on securitised underlying exposures could support the mainstreaming of ESG? Which underlying exposures would that impact?

Please see answer to question 35 above.

39. Do you have any views on how the Sec Reg can better support the government's aims for green finance in the near future?

Please see answer to question 35 above.

THIRD PARTY VERIFICATION REGIME

40. When making investment decisions, how important is it to you that the compliance with the STS criteria is verified by a TPV? Please explain why.

For public deals and initial issuances, it's important to us that the STS criteria is verified by a TPV, primarily due to the comfort afforded by an independent third party verifying the required criteria. However, if a well-known, sophisticated issuer has multiple, repeat transactions (ie same asset class, broadly on the same terms / structure, like an auto deal), we are more agnostic as to whether that issuer repeatedly obtains the services of a TPV.

41. Do you think the TPV regime under the Sec Reg is appropriate? In particular: a. What are your views on the impact of the authorisation process for TPVs on the level of competition in the market? b. What do you think could help foster competition? c. Given the role that TPVs play in the STS market and the current number of authorised TPVs, do you think there might be any risk of harm arising from over-reliance on the assessment of a TPV? d. Do you think the TPV regime should be amended to address those risks?

Broadly speaking, we feel that the TVP regime is appropriate, working well and cost effective. We would be concerned if the cost of using a TPV increased as this could discourage an issuer from using their services. We feel that the implementation of and adherence to the Sec Reg has already increased deal costs, especially for private deals and SMEs, so would be vary of unnecessary increased expenditure.

THE ROLE OF SSPES

42. SSPEs have specific obligations under Article 7 to ensure sufficient provision of information to investors. Do you consider this information to be sufficient to be able to ascertain a full view of the transactions, including the level of interconnectedness of institutions (if so desired)?

We feel the current regime works well and have had no issues procuring information from the applicable party.

43. Do you think that this will be improved by the existence of authorised SRs?

No. We feel that the current regime works well and would object to the existence of authorised SRs. We feel this would increase costs, complexity and time especially for private transaction and SMEs.

Additionally, Insight Investment also requests additional information from SSPEs, originators and sponsors, on a deal by deal basis, so it is important that there is a direct line of communication. Our investment deal teams do require direct communication to undertake their credit analysis and this could be hindered by the use of an SR.

44. As an originator/sponsor/investor, how many SSPEs do you interact with on a per transaction/programme basis?

Typically, for European / UK deals Insight Investment interact with just one SSPE per transaction. For some US originator / sponsor deals (notably in the CLO market) transactions are structured with two SSPEs.

45. Do you have any concerns with the robustness of the SSPE regime regarding its ability to: a. ensure it is insolvency remote; and b. ensure it has sufficient funds to continue operations (both generally and in the context of an enforcement or acceleration notice)?

Putting to one side the inherent legal and operational risk of any transaction (securitisation or otherwise), we do not have any concerns with the robustness of the SSPE regime regarding its ability to: a. ensure it is insolvency remote; and b. ensure it has sufficient funds to continue operations (both generally and in the context of an enforcement or acceleration notice).

46. Should HM Treasury introduce a system of LLBs to replace and centralise the functions of SSPEs?

No, we would oppose such an introduction if a system of LLBs was made mandatory and used to replace and centralise the functions of SSPEs. The use of SSPEs is well established with market participants familiar with the legal, tax, insolvency licensing and regulatory regime.

We feel that the introduction of a system of LLBs in the UK (if their use was mandatory) would discourage market participants from establishing the 'SSPE' in the UK and would revert to offshore jurisdictions.

As a final point, the tax regime of UK SSPEs has now been adopted (and consulted on) by the UK Treasury and we feel market participants are comfortable with the use of SSPEs.

ALTERNATIVE INVESTMENT FUND MANAGERS – EXTRATERRITORIALITY

47. Do you have any comments on HM Treasury's views regarding the definition of institutional investor under the Sec Reg, as it applies to AIFMs?

Not applicable. No comment.

48. What are the practical effects of the due diligence requirements for nonUK AIFMs managing or marketing in the UK?

Not applicable. No comment.

49. Are there any perceived benefits of the extraterritorial requirements?

Not applicable. No comment.

50. Do respondents have any concerns with amending this definition? Would this risk any unintended consequences that HMT should be aware of?

Not applicable. No comment.